

**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

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| Date Amended: | 04/12/07 | Bill No: | <u>AB 1094</u> |
| Tax: | Diesel Fuel Tax | Author: | Arambula |
| Related Bills: | | | |

BILL SUMMARY

This bill would allow an ultimate vendor or licensed supplier of diesel fuel to claim a specified per-gallon reimbursement for tax-paid, clear diesel fuel sold to an ultimate purchaser for use on a farm for farming purposes.

SUMMARY OF AMENDMENTS

The amendments since the previous analysis clarify that the reimbursement does not apply to tax-paid, clear diesel fuel sold to an ultimate purchaser for use in an exempt bus operation and that it applies only to diesel fuel sold on or after January 1, 2008. The amendments also specify that the reimbursements would be appropriated from moneys deposited in the Motor Vehicle Fuel Account in the Transportation Fund.

CURRENT LAW

Under existing Diesel Fuel Tax Law (Part 31, Division 2 of the Revenue and Taxation Code, commencing with Section 60001), the state imposes an excise tax of \$0.18 per gallon on the removal of diesel fuel at the refinery or terminal rack, upon entry into the state, and upon sale to an unlicensed person, unless specifically exempted.

There are two methods by which farmers may purchase diesel fuel for use on a farm for farming purposes without paying the diesel fuel tax. A farmer may purchase dyed (untaxed) diesel fuel if, among other things, the fuel will be used exclusively for nontaxable, off-highway purposes, such as on a farm, or the farmer may purchase undyed (tax-paid) diesel fuel from an ultimate vendor without paying the diesel fuel tax, if that fuel will be used on a farm for farming purposes.

Sales of dyed diesel fuel for off-highway use. Specifically exempted from the payment of the tax is diesel fuel that satisfies specified dyeing and marking requirements. Dyed diesel fuel is diesel fuel that is dyed pursuant to United States Environmental Protection Agency (EPA) and Internal Revenue Service (IRS) rules for high sulfur diesel fuel or low sulfur diesel fuel, or any other requirements subsequently set by the EPA and the IRS, and considered destined for nontaxable, off-highway uses. No person may operate or maintain a motor vehicle on any public highway in this state with dyed diesel fuel in the fuel supply tank, unless otherwise specified.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

Sales of undyed diesel fuel for use on a farm for farming purposes. Section 60502.1 provides that an ultimate vendor shall not include diesel fuel tax in the sales price or on the sales invoice for diesel fuel sold to an ultimate purchaser. Under Section 60502, any ultimate vendor who has paid a tax on diesel fuel sold to an ultimate purchaser for use on a farm for farming purposes may be reimbursed for the amount of diesel fuel tax paid. To obtain reimbursement for the amount of diesel fuel tax paid, an ultimate vendor must file a claim for refund with the Board, as specified.

Section 60036 defines an “ultimate vendor” to mean a person that sells undyed diesel fuel to the user of the diesel fuel (the ultimate purchaser) for use on a farm for farming purposes or for use in an exempt bus operation. Section 60037 defines an “ultimate purchaser” to mean a person that uses diesel fuel for use on a farm for farming purposes or an exempt bus operator that uses diesel fuel in an exempt bus operation.

Refunds for tax paid for diesel fuel used on a farm for farming purposes. Section 60501 specifically prohibits any person who has paid a tax on diesel fuel used on a farm for farming purposes from being reimbursed for the amount of the tax paid through the claim for refund process.

Disposition of funds. Section 60651 requires the Board to transmit all money received under the Diesel Fuel Tax Law, except as specified, to the Treasurer to be deposited in the State Treasury to the credit of the Motor Vehicle Fuel Account in the Transportation Fund. Section 60652 states that all moneys deposited in the account are continuously appropriated, without regard to fiscal year, to pay authorized refunds, and the balance of the moneys are transferred to the Highway Users Tax Account in the Transportation Tax Fund.

PROPOSED LAW

This bill would add Section 60502.3 to the Revenue and Taxation Code to allow an ultimate vendor or a licensed supplier to claim reimbursement for the costs associated with filing the claim for refund of the tax paid on, or claiming a credit for, diesel fuel sold to an ultimate purchaser for use on a farm for farming purposes. The reimbursement would be in addition to the refund of the tax paid on, or the credit for, diesel fuel sold to an ultimate purchaser. The reimbursement rate would be set at a rate of two and one-half cents (\$0.025) per gallon on the gallons of diesel fuel sold to an ultimate purchaser and claimed on an ultimate vendor’s claim for refund filed electronically with the Board or claimed as a credit in lieu of a refund on the supplier’s tax return filed electronically with the Board. These provisions would apply only to diesel fuel sold to an ultimate purchaser on or after January 1, 2008.

This bill would also amend Section 60652 to provide that the moneys deposited in the Motor Vehicle Fuel Account in the Transportation Fund would be continuously appropriated, without regard to fiscal years, to pay authorized reimbursements for the costs associated with filing the claim for refund of the tax paid on, or claiming a credit for, diesel fuel sold to an ultimate purchaser for use on a farm for farming purposes.

This bill would become effective January 1, 2008.

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BACKGROUND

On August 10, 2005, President Bush signed H.R. 3, which is known as the Safe, Accountable, Flexible, and Efficient Transportation Equity Act of 2005, into Public Law (Public Law No. 109-59). Among other things, Public Law No. 109-59 repealed the federal law that permitted ultimate vendor refund claims with respect to farming. This change in federal law applies to sales after September 30, 2005.

Last year, two bills related to tax-paid diesel fuel sold for use on a farm for farming purposes were considered; AB 674 (Klehs) and AB 2981 (La Malfa). AB 674 would have revised the method by which the excise tax on tax-paid diesel fuel used on a farm for farming purposes is refunded. That measure was refused passage out of the Assembly. AB 2981 would have 1) exempted from the diesel fuel tax the storage, use, or other consumption in this state of diesel fuel used in farming for a farming purpose when such fuel is removed from a terminal rack, 2) required a farmer that is an "ultimate purchaser" to remit any underpayment of diesel fuel tax to the Board, and 3) allowed a farmer that is an "ultimate purchaser" to file for a refund for any overpayment of estimated diesel fuel taxes based on the use of fuel for non-farming purposes. That measure died in the Assembly Committee on Revenue and Taxation.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the California Independent Oil Marketers Association (CIOMA) and is intended to be a cooperative solution between California's farming community and fuel marketers, with all parties interested in strengthening the state's agricultural industry as a whole.

According to the sponsor, "The financial and administrative burden on independent marketers, known as jobbers, is significant, and this situation places unnecessary stress upon an industry that is critical to the vitality of agricultural economies. Jobbers contribute an invaluable service to the rural and agricultural regions of California, providing the energy necessary to work the state's fields and harvest the state's food."

2. **Summary of amendments.** The **April 12, 2007, amendments** add Board suggested language to 1) clarify that the reimbursement does not apply to tax-paid, clear diesel fuel sold to an ultimate purchaser for use in an exempt bus operation, 2) state that the reimbursement provisions apply only to diesel fuel sold on or after January 1, 2008, and 3) specify that the reimbursements would be appropriated from moneys deposited in the in the Motor Vehicle Fuel Account in the Transportation Fund.
3. **This bill should contain a specific appropriation to the Board.** This bill would allow suppliers and ultimate vendors to claim a reimbursement for their costs commencing on January 1, 2008. However, implementation of the bill's provisions would begin prior to January 1, 2008, which is in the middle of the state's fiscal year. In order to begin to revise reporting and claim for refund forms and to develop computer programs, an adequate appropriation would be required to cover the

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Board's administrative start-up costs that would not already be identified in the Board's 2007-08 budget.

Constitutional and statutory provisions prohibit the Board from using special fund appropriations to support the administration of the diesel fuel tax program. Without an appropriation for administrative start-up costs, the Board would have to divert **General Fund** dollars to the diesel fuel tax program, which would have a negative impact on the revenues of State and local government.

As an alternative to an appropriation, the author may want to consider amending the bill to move the operative date to January 1, 2009. This would allow the Board to obtain funding for administrative start-up costs through the Budget Change Proposal process.

4. **What other Board-administered programs provide reimbursement?** Authorizing suppliers and ultimate vendors to retain a per-gallon rate as reimbursement for the costs associated with filing the claim for refund (or claiming a credit) for diesel fuel sold to an ultimate vendor could set a precedent for other taxes and fees administered by the Board. Of the 25 revenue-generating tax and fee programs administered by the Board, reimbursement is only allowed under the California Tire Fee Law, the Electronic Waste Act of 2003 (covered electronic waste recycling fee or Ewaste fee), and the Cigarette and Tobacco Products Tax Law.

The California Tire Fee Law authorizes a retail seller to retain 1.5 percent of the fee as reimbursement for collection costs. The fee is imposed on the consumer, but required to be collected by the retail seller. Similar to the California Tire Fee Law, the Electronic Waste Act of 2003 imposes the Ewaste fee on the consumer and is required to be collected by the retail seller. Under that program, a retail seller is authorized to retain 3 percent of the fee as reimbursement for collection costs. And lastly, the Cigarette and Tobacco Products Tax Law provides that cigarette tax stamps are to be sold to licensed distributors at a discount of .85 percent of their denominated value, which is intended to help defray the cost (leasing of equipment/labor cost) to the distributor for affixing the stamps. This measure proposes a reimbursement to a supplier or ultimate vendor in an amount equivalent to approximately fourteen percent (14%) of the diesel fuel tax refunded.

COST ESTIMATE

The Board would incur non-absorbable costs associated with this bill to inform suppliers, ultimate vendors and ultimate purchasers, program computers, and revise returns and claim for refund forms. A cost estimate of this workload is pending.

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REVENUE ESTIMATE**BACKGROUND, METHODOLOGY, AND ASSUMPTIONS**

The Board's Fuel Industry Section reports that in 2006, ultimate vendor and diesel supplier return claims were 63.3 million gallons for use on a farm for farming purposes.

If we apply the proposed reimbursement cost of \$0.025 per gallon to the 63.3 million gallons consumed in 2006, total estimated reimbursements costs would be \$1.6 million (63 million gallons × \$0.025 = \$1.6 million)

REVENUE SUMMARY

This bill would result in an estimated revenue loss of \$1.6 million annually.

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